REPORT OF THE COMMITTEE ON FOREIGN TRADE

This, the second report of the Committee on Foreign Trade, will cover the effect of the war on the volume, direction, and the constituent commodities of international trade, and will attempt to analyze some of the conditions that affect the outlook.

I. The Effects of the War

The war had a very profound effect upon the trade of the world. In belligerent countries normal production was curtailed and therefore exports declined. The domestic production of commodities needed by the warring nations was insufficient and these had to be imported. The excess of imports was financed by shipments of gold, the sale of securities, and by borrowing. The trade currents prevailing before the war were upset.

A. *The Volume of Trade.*—The countries at war greatly increased their exports in amount and to a less extent in tonnage. The countries on the American continent on the whole greatly increased their exports. Japan did likewise. The countries blockaded, Germany and Austria, experienced a tremendous decline in trade. The trade of Holland, Spain, and Russia declined as an incident to the blockade. Because of the long sea voyage involved and the shortage in shipping, the trade of British India, Australia, and South Africa also fell in volume.

B. *Commodities of Trade.*—Because the belligerents of Europe needed enormous quantities of war materials and other goods for consumption, their imports of manufactures increased relatively and the imports of raw material decreased relatively. Western Europe was cut off from its sources of food supply in Russia and Southeastern Europe, and the entire burden of producing food for the Western European countries was thrown upon the Americas. Australia and India were too far removed to permit the utilization of much needed tonnage for the long ocean trip. Because Germany was under blockade, the countries which she had supplied with chemicals, dye-stuffs, porcelain, machinery, electrical goods, toys, and specialties had to turn to other countries like Switzerland, the United States, and Japan for their supply. Trade in luxuries was much reduced. Japan, the United States, and in general the neutrals increased their imports of raw materials and increased their exports of manufactured goods.

There was an increased demand for commodities of all kinds from countries that were readily accessible to Europe, and they, therefore, suffered from a shortage of goods. On the other hand, the demand upon the countries far removed from Europe slackened so that there was a glut of goods, as of wheat in Australia, wool in New Zealand, and sugar in Java.

C. *Trade Currents.*—The war resulted in the transfer of millions of men to France, where they had to be maintained under conditions which increased their consumption over that of peace. Shipping routes were therefore focused upon Western Europe and created a

ship shortage in other lanes of trade, which was aggravated by submarine warfare. The tonnage passing through the Suez Canal in 1913 was 20,000,000 tons and in 1917 only 8,300,000 tons. Because of the shortage in shipping, supplies for Europe had to be brought from the nearest available center of production. Tonnage was conscripted for the trans-Atlantic service. There was an increase of exports to Europe and a decrease of imports from Europe.

Furthermore, trade between nearby countries increased; for example, the trade among the northern neutrals of Europe, between Japan and the countries skirting the Pacific and Indian Oceans, between the United States and the countries of North and South America and of Asia. The trade on the Pacific greatly increased. The countries of Asia, East Africa, and the west coast of the Americas traded with each other to a greater extent than before the war.

Because of the shortage in shipping, heavy commodities were eliminated to a large extent and wherever possible home sources of supply were developed. The lack of those goods which were manufactured chiefly in Central Europe stimulated the establishment of new branches on industry in the non-European countries.

D. *Entrepôt and Transshipment Trade.*—The European countries which were at war had controlled the shipping of the world and determined the course of commodity movements. Trade prestige and established custom were important determinants of the route of trade and of the location of entrepôt centers before the war. During the war, the blockade and economy of shipping were the deciding factors. American cotton was sent to Holland direct instead of by way of Bremen and Liverpool. Dutch colonial produce reached the United States directly, instead of by way of Amsterdam. African produce could no longer be shipped by way of Belgium or France. The United States obtained Australian goods across the Pacific and not by way of London. Trade routes which were temporarily expedient have in some cases proven to be permanently efficient.

Hamburg and Bremen were closed tight during the blockade and the transshipment and entrepôt trade which they had conducted were eliminated. The European countries which had traded with the outside world through the medium of Germany now traded directly. The trade of Switzerland, Italy, the Baltic States, and Spain, with the overseas countries, greatly increased. Furthermore, new centers of transshipment developed during the war. Copenhagen, Bergen, and Goteborg rose as ports of transshipment and as entrepôts supplying Germany and the north of Europe.

E. *Economic Decentralization.*—For four years the countries dependent upon Europe have been compelled to seek new sources of manufactured goods and new outlets for their raw materials, or else to establish some local industries to satisfy their needs. The industries of the world, hitherto concentrated chiefly in Europe, have been temporarily disrupted and to some extent permanently decentralized. The transshipment of goods from the Orient to America or from South Africa to North America by way of Europe has been partly

replaced by direct trade. The international jobbing business has been reduced and in some lines eliminated. Countries were compelled to become self-sufficient. The old creditor nations, clustered in Europe, have become borrowers of widely scattered countries, as the United States, Japan, and Argentine, hitherto their debtors. The world has hastened toward a state of economic development which it might have taken generations to attain. The predominance of Europe in trade has declined, and new commercial spheres have become defined in America and in the Far East, centering about the United States and Japan.

Agricultural countries and regions producing raw materials develop eventually into centers of industry and trade. The war hastened this process. It has hastened the growth of industrial self-sufficiency, the decentralization of trade, and the lessened dependence upon Europe of the rest of the world. The war has hastened the disintegration, not only of political imperialism, but of commercial imperialism as well.

Decentralization is the prerequisite of federalism. In a more than superficial sense, therefore, the war has prepared the world for an inevitable league of nations of some sort. As the backward countries of the world become more industrialized, as the density of their population tends to increase by migration, the economic dominance of Europe will probably decline still further but the interdependence of the nations of the world will increase. The process of economic decentralization will prepare for ultimate world federalism. More extensive interdependence of the nations will vitalize a league of nations.

II. The Outlook in International Trade

A. *The Pre-war Balance of Trade.*—Before the war the countries of Europe, with the exception of Russia, had an excess of imports. On the other hand the countries of the American continent, with the exception of Canada, and most of the partly developed countries such as British India and South Africa, had an excess of exports.

The excess of imports of the European countries was paid for by services, such as shipping and banking, by interest on foreign investments, by the expenditures of non-European tourists in Europe, and by the remittance of European nationals in foreign countries to their friends and families in Europe.

B. *The War-time Balance of Trade.*—The countries of Europe, on the whole, increased their imports greatly. The non-European countries on the other hand had a large excess of exports, particularly during the later years of the war.

Europe paid for the increased excess of imports less by banking and shipping services, more by the shipment of gold, and the sale of securities, and most of all by loans.

C. *The Immediate Future.*—1. Europe needs credit.—Europe in part is devastated and everywhere is short of goods. The war-ravaged countries need food and machinery. But even the neutrals need raw

materials. Without food and raw materials Europe must have goods and to get them she needs our credit.

But for purely selfish reasons we must lend. In order to balance our international debits and credits, the courses before us are to curtail exports, increase imports, or to lend. Reduction of our exports seems inevitable. However, to curtail our foreign sales suddenly would mean stagnation of industry and consequent unemployment in many lines, although in some cases the satisfaction of demands at home deferred during the war would absorb the slack in production as prices decline. We cannot at present buy more, for Europe has less to sell now than before the war. As a temporary expedient the course open to us is to lend. For the economic welfare of the country credits of some sort must be advanced in order to move American goods.

2. The supply of short-term credit.—Some European statesmen thought that they could borrow from America sufficient funds to restore the devastation quickly. Unfortunately, that is not the case. The credit needed is of two kinds, long-term and short-term. The neutrals and the belligerents not devastated by the war will not need long-term credit to any great extent. The machinery for supplying short-term credit for exports consists of the facilities afforded by the Federal Reserve system. However, should a scarcity of short-term credit for exporters arise, there are untapped reserves in the discount houses which may accept drafts up to several times their capital. To a great extent these institutions would relieve the banks of deposit of the risk of too heavy commitments on account of foreign acceptance liabilities in addition to their ordinary commercial risks. Several of these have been established.

3. The supply of long-term credit.—Six months' credit, even with a renewal, would hardly provide for the needs of countries in which factories and even cities will have to be rebuilt, and reëquipped.

a. Government advances.—During the war the United States government made advances to other governments to the extent of about $10,000,000,000. These advances cease with the proclamation of peace. The sentiment in the United States is averse to further loans by our government. Our government has a floating debt of over three billions. This is a revolving debt and is responsible in part for the inflation of prices and the high cost of living. The government could loan to Europe by issuing more bonds. Congress would hardly authorize such loans and the public would hardly take such loans if authorized. Conceivably conditions in Europe might compel a change of sentiment in the United States. The evils of inflation may be less menacing than industrial debility in Europe attended perhaps by political disturbances.

b. Indirect government aid.—The United States has, however, undertaken to aid the exporter indirectly, through the War Finance Corporation, which may make advances to the extent of $1,000,000,000 for periods of not exceeding five years, to exporters or bankers upon the promissory notes of the borrower. However, the difficulty in-

herent in the act under which the War Finance Corporation operates is that while the country as a whole benefits by the export of goods, the burden of the present unusual risk is placed entirely upon the exporter. Nevertheless, the facilities of the Corporation are being utilized.

c. Private means.—The financing of foreign trade by the government may lead to further inflation. The financing of exports through private channels can be accomplished only through savings, past or present. The alternatives of war financing, namely, inflation versus savings, face us again during the transition. Possibly the gravity of the after-war stiuation may compel a compromise as in war time between these two methods of financing.

At present Europe is being financed by private income. Private aid is being extended to individual enterprises, whose conditions meet the credit standards of bankers. The methods of private long-term finance are various. Either Europe's holdings of neutral securities might be liquidated in the United States or else a foreign importer, if his credit is good, might float a loan here.

The member banks of the Federal Reserve system have been permitted to invest 5 per cent of their capital and surplus in subsidiary corporations engaged in the financing of foreign trade. The Edge Law authorizes the establishment and the incorporation under federal charter of companies to engage in international financial operations under the supervision of the Federal Reserve Board.

Furthermore, investment trusts might be established. These institutions would invest in foreign securities and issue their own obligations against their holdings, which might be either government bonds, industrials of the borrowing country, or the pledged securities of a third country or of its industries.

Finally, the listing on the stock exchange in the United States of outstanding foreign securities, under proper restrictions and with adequate safeguards of the American investors, would help greatly in accelerating the flow of trade.

d. The essentials of an acceptable foreign security.—If advances are to be made to countries fiscally weak, or to industries already under heavy taxation charges, a priority of lien will be needed to assure the safety of interest and principal of the new loan as compared with the old ones. If new loans to weak countries are to be junior liens, funds for Europe will be difficult to obtain. Just as a private company that has good prospects may secure credit through the issue of receiver's certificates, so the weak European countries will have to give priority of lien of principal and interest of new money as against old loans.

The rate of interest on loans to foreign governments or industrials will have to be competitive with domestic rates. The marketability of securities based on foreign loans depends upon suitable publicity, and whether or not the public will avoid waste and gather funds for investment, and whether or not they are favorably disposed toward the investments from the viewpoint of safety and adequacy of return.

In order not to be the lone and sole creditor of the nations of Europe, the United States might raise a loan jointly with other powers, or with the participation of other powers to a sufficient extent morally to insure payment by the borrower. The endorsement of the European banker, and the guarantee of the foreign government may be essential to secure the funds from American investors.

Such credits as are granted to Europe should be devoted to industrial and not governmental uses. They should be utilized not for meeting current government expenses, not for the balancing of their budgets where there is a lack of adequate measures of taxation, and not for the artificial maintenance of their inflated currencies at parity in the exchange market. Credits should be devoted to increasing production. The import into Europe of essentials and not of luxuries should be financed. If industry in Europe is benefited the security underlying our loans, new and old, will be strengthened. As industry in Europe revives, world-wide economic conditions should benefit.

D. *The Outlook in the United States.*—What is to be the future of our foreign trade? The theoretical analysis indicates that during the early stages of lending, a country has an excess of exports. After this process has continued for many years, the lending country has an excess of imports.

Our present position has been obtained not as a result of the slow process of economic development, but as a result of the sudden shifting of trade during the war. However, our readjustment cannot be as sudden. It will take years. Europe took our exports and gave us promissory notes in payment. She cannot liquidate her debt in gold, because European countries wish to retain their gold supply in anticipation of a return to a gold basis. Because of the development of American facilities for financing trade and because of the creation of the American merchant marine, Europe will not be able to pay us with these services even to as great an extent as before the war. Securities with which to pay us are either not available or else will not be sold by Europe because of the commercial prestige which attaches to foreign investments.

Ultimately, Europe must pay us in goods. A mortgage on her fixed assets is not feasible politically, because of the anti-alien laws of Europe and the fear of economic penetration. Europe will therefore eventually have to pay in merchandise. The annually accruing interest on the debt to the United States will depress the exchange rate of the debtor country and thus stimulate exports and restrict imports. On the other hand, the annual credit of the United States for interest will tend to raise our exchange above par, to stimulate imports and to restrict exports. Ultimately our excess of exports must decline and probably change to an excess of imports—a feature which before the war characterized the trade of the creditor countries of Europe.

Immediately, Europe may be unable to pay in goods. Her debt to us for interest must be postponed, or met temporarily by further loans to her. The need of additional goods from America will need to be

financed in the same way. Loans by us would make possible a continuation of our exports until the productive capacity of Europe is restored sufficiently to permit the resumption of exports by Europe. The annual investment of a sum equal to our excess of imports and the reinvestment of the interest on loans, both outstanding and to be placed, would, if compounded, reach a huge figure in a generation. Our balance of trade would thereafter probably be an excess of imports.

In the present unsettled state of Europe there are many factors which would qualify these conclusions. If Europe falls into chaos, exports from the United States will be greatly reduced. If the principal and interest of our present loans is thus wiped out, the conditions which would call for an ultimate excess of imports will cease to exist.

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